

Turkey's Choice in Iraq: Burned Bridges or Win-Win-Win

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Brief Analysis

The next six months could see either a game-changing strategic energy compact between Turkey and the Iraqi Kurds or movement toward a more sustainable Ankara-Baghdad-Erbil relationship. Washington has a strong interest in encouraging the latter.

Building sustainable relationships between Turkey, Iraq, and the Kurdistan Regional Government (KRG) is of critical importance to U.S. security and economic interests in the region. Turkey has hinted that it is considering high-volume oil and gas imports directly from the KRG -- a move that could burn Ankara and Erbil's bridges with Baghdad. Other developments point to the beginnings of U.S.-brokered reconciliation between Turkey and Iraq. Such a rapprochement could reanimate hopes for a "win-win-win" solution whereby KRG hydrocarbons are exported via Turkey using existing federal Iraqi infrastructure and legal mechanisms, with reliable revenue sharing and cost recovery reaching the KRG and its oil contractors via the federal exchequer. With Turkish prime minister Recep Tayyip Erdogan visiting the White House on May 16, the next month may constitute a fork in the road. Whatever the case, all parties should work assiduously to exploit the last window of opportunity with the current Iraqi government, whose term ends next year.

Turkey-KRG negotiations

Turkey has two main options for developing its energy relationship with the Iraqi Kurds this year. First, the Turkish Petroleum International Company (TPIC) could invest in the KRG's upstream oil sector in the same way that ExxonMobil, Chevron, Total, and scores of other firms have done. This option, which has firm support throughout the Turkish government, is more of a "tactical" approach -- that is, Turkish firms may seek profitable investments in northern Iraq, but Ankara would stop short of leveraging Turkey's geographic position as a potential export route for KRG hydrocarbons.

Alternatively, Ankara could agree to a game-changing "strategic" energy compact with the KRG, with Turkey receiving high-volume Kurdish oil and/or gas exports independently of Baghdad. In that scenario, new pipelines would need to be built within Turkey and the KRG. Likewise, novel and legally untested marketing and financial arrangements would be required to monetize the resources, since the arrangements normally proffered by the State Oil Marketing Organization of Iraq would not apply if Baghdad were circumvented.

Turkey has hinted at its interest in certain aspects of this strategic option. In January, Foreign Ministry undersecretary Feridun Sinirlioglu raised the prospect of a bilateral Turkish-KRG gas pipeline during a visit to Washington. And after meeting with KRG prime minister Nechirvan Barzani on March 25, Erdogan confirmed that Turkey had signed a "trade agreement" with the Iraqi Kurds; oil industry analysts believe the pact includes agreement-in-principle on pipelines, revenue sharing, and high-volume oil and gas imports from the KRG. On April 4, Turkish energy minister Taner Yildiz added that Ankara would be prepared to administer an 83-17 percent payment split between Baghdad and Erbil for KRG-derived oil exported through Turkey -- an unorthodox arrangement that would effectively remove sovereign marketing and fiscal responsibilities from Baghdad. On April 6, as Secretary of State John Kerry visited Ankara, the KRG announced that it had sold its first cargo of crude oil on the international market, delivering 30,000 tons that had accrued at storage facilities on Turkey's Mediterranean coast. Erbil plans to transfer the resultant funds to a Turkish refining company that provides fuel products to Iraqi Kurdistan, allowing the KRG to claim that the sale is part of a barter scheme.

IMPLICATIONS FOR U.S. POLICY

Since the breakdown in relations between Erdogan and Iraqi prime minister Nouri al-Maliki in 2011, Washington has rightly sought to prevent the schism from pushing Turkey into an exclusive energy relationship with the KRG at Baghdad's expense. Encouraged by U.S. diplomats, Iraq has recently taken steps to open the door for reconciliation. On the eve of Kerry's Ankara visit, Maliki's press office released a statement noting that "Iraq welcomes any step toward rapprochement with Turkey on the basis of shared interests, mutual respect, and good-neighborliness." More concretely, Baghdad has discussed new pipeline deals with Ankara, such as connecting Basra's super-giant oil fields and major new gas flows to Turkey. The initiative drew positive comments from Yildiz; on March 31, he stated, "We are ready to transfer the crude from Basra to world markets when needed...We will begin the project when our Iraqi brethren are ready."

Yildiz's statement hints at the crux of the matter: the need for effective follow-up and implementation, which is where Washington can contribute. Even before the Maliki-Erdogan schism -- sparked by Ankara's overt support of Maliki's opponents in Iraq's 2010 election and fanned into a public conflagration between the leaders a year later -- the Turkish government had justifiably grown tired of Baghdad's apparent inability to push forward joint energy initiatives. Washington convinced the two countries to sign a broad economic cooperation agreement in 2009, but the 2011 breakdown in relations impeded further progress. With U.S. support, Baghdad should be more proactive in engaging Turkey on a major energy project.

For example, Ankara has long sought greater Iraqi exports as part of its effort to become an energy hub and increase transit fees through full exploitation of the underutilized Iraq-Turkey Pipeline (ITP). Erdogan's March 29 interview with CNN Turk included specific reference to "making the existing pipeline more active," and Yildiz has frequently emphasized Ankara's preference to bring the ITP up to full capacity before building any new pipelines for KRG-derived oil. Indeed, Turkey, Iraq, and the KRG -- not to mention the United States and world oil markets -- stand to benefit greatly if more Iraqi oil (and, eventually, gas) can flow north via Turkey, reducing overdependence on Basra export facilities and the Strait of Hormuz. To maintain momentum toward expanded energy relations between Ankara and Baghdad, Washington should facilitate leadership conferences and technical workshops on Basra-Turkey pipeline systems and repair of the ITP.

At the same time, the United States should pressure Baghdad to readdress formalized revenue sharing, starting with budgetary allocations to provide cost recovery for KRG contractors. Ideally, a supplemental or reissued budget will be negotiated as quickly as possible; it should include a goodwill gesture to reduce the multiyear arrears owed to KRG contractors (e.g., a substantial lump sum payment of at least \$500 million), as well as monthly installments of around \$250 million. The latter step would allow Erbil to begin feeding significant volumes of oil (i.e., 200,000 barrels per day) into the federal system at the agreed cost-recovery rates brokered in the Baghdad-KRG deal of September 2012. If effective, this temporary system could kickstart work on a lasting revenue-sharing law for Iraq. Turkey and the KRG are convinced that formalized revenue sharing -- rather than the existing system of budget-by-budget allocations -- is the solution to the ongoing impasse, and putting U.S. weight behind the idea is one way to keep them engaged with Baghdad.

Getting in the game is also a way to demonstrate that Washington can do more than shout from the sidelines. Hectoring Ankara and Erbil using old talking points is not the best means of preventing exclusive Turkish-KRG energy relations; a better option is to change their strategic calculus by facilitating better alternatives. This means getting Iraqi-Turkish energy relations back on track and keeping the Baghdad-based cost-recovery system operational for the long term -- the only viable route to the win-win-win scenario that is best for all parties, including the KRG.

Michael Knights is a Boston-based Lafer fellow with The Washington Institute. ❖

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